UNITED
NATIONS

TD

United Nations Conference
on Trade and Development

Distr.
GENERAL

TD/B/CN.4/23
27 August 1993

Original: ENGLISH

TRADE AND DEVELOPMENT BOARD
Standing Committee on Developing Services
Sectors: Fostering Competitive Services
Sectors in Developing Countries
Second session
Geneva, 11 October 1993
Item 5 of the provisional agenda

FOSTERING COMPETITIVE SERVICES SECTORS

A COMPARATIVE ANALYSIS OF SERVICES SECTORS IN DEVELOPING COUNTRIES

(Item 3 (a) of the work programme)

Prepared by the UNCTAD secretariat

GE.93-53046 (E)

CONTENTS

	Paragraphs
Introduction	1 - 3
Part One: Comparative Analysis of the Service Situation in Developed and Developing Countries	4 - 32
I. The Strategic Role of Services in Developed and Developing Countries	5 - 19
A. The traditional role of services	5 - 7
B. The developed countries and the "services revolution"	8 - 15
C. The new service economy and the developing countries	16 - 19
II. Producer Services in Developing Countries	20 - 32
A. Demand for producer services	26 - 28
B. Main characteristics of the supply of producer services	29 - 32
Part Two: Components for a Policy of Strengthening Services in the Developing Countries	33 - 84
I. Domestic Strategy	33 - 59
A. Context	33 - 46
B. General framework	47 - 51
C. Specific strategies	52 - 59
II. External Strategy for Developing Internationally Competitive Sectors	60 - 84
A. How to penetrate world markets: Improving conditions of access to the international market	60 - 72
B. Increasing participation of developing countries in international markets: Elements of a strategy	73 - 84
Concluding Remarks	85

Boxes in the text

1. Grouping of Producer Services According to the Production Function

2. Producer Service Centres: An Example

INTRODUCTION

1. Item 3 (a) of the Work Programme instructs the Standing Committee to "conduct a comparative analysis of service sectors in developing countries; such analysis will: (i) examine the role played by services in contributing to growth and sustainable development, including an examination of the contribution of the producer services sector in facilitating the competitiveness of goods-producing sectors, and to the economy as a whole; (ii) assess weaknesses and capabilities; and (iii) identify policies to assist developing countries in developing and strengthening their competitive services sectors, including infrastructure relating to services."

2. The secretariat has prepared this background note with a view to facilitating the work of the Committee in this regard. It is primarily a synthesis of the findings of work carried out in UNCTAD. The note has been guided by the Cartagena Commitment which clearly recognized the need for developing countries to pursue policies to create appropriate conditions for the development of their national services sector and encouraged the international community to support the efforts of national Governments to strengthen the production and export capacity of the sector. The purpose of this note is to provide a point of departure for further work under this sub-item, as well as for the various studies to be prepared under other items of the Work Programme of the Standing Committee. The identification of policies, envisaged under (iii) above, is expected to emerge as a result of this process.

3. The note draws heavily upon previous work carried out in UNCTAD in a series of national, regional and sectoral studies on services. While not constituting a systematic investigation of service sectors in developing countries, they were specific responses to a variety of needs of individual countries and regions, limited by the objectives of individual projects and the extent of financial resources. This is reflected in the note. The recommendations made are of necessity tentative, mainly aimed at assisting the Committee in determining the orientation of future work with respect to analysis and policy options.

PART ONE

COMPARATIVE ANALYSIS OF THE SERVICE SITUATION IN DEVELOPED AND DEVELOPING COUNTRIES

4. In terms of their contribution to the growth and sustainable development of countries and the contribution made by producer services to the competitiveness of the goods sectors and to the economy as a whole, services perform a central function in the adjustments which economies have had to make in order to gain a competitive position in the world economy. This has given services a new strategic role that transforms them into decisive factors in the generation of value added to the economy and in the creation of competitive advantages. This chapter compares the situation of services in developed and developing countries and identifies the main features, elucidating the strengths and weaknesses of developing countries in this matter.

I. The Strategic Role of Services in Developed and Developing Economies

A. The traditional role of services

5. The provision of physical infrastructural services such as telecommunications, transportation and essential utilities, together with social infrastructure such as health, housing and education, as well as the availability of financial services have traditionally formed an integral part of national development strategies. Policies with respect to these sectors have been strongly influenced by considerations of national security, attainment of particular strategic objectives, ensuring the widest possible access of the population to essential services, and providing the necessary infrastructure for various economic activities. These considerations have led Governments to assume a major role in services provision as well as in regulating it. The need to reconcile this complex set of objectives with that of economic efficiency raises a dilemma.

6. As considerations of economic efficiencies and international competitiveness have become predominant, this dilemma has become more acute. There is an increasing awareness that inefficiencies arising in the provision of any basic service necessarily affect the competitiveness of firms using that service. This has called into question the role and priorities of Governments and the need for new forms of regulations. The concern for ensuring quality, reasonable prices and adequate coverage of a service, while at the same time adapting it to technological advances, places the service supplier under pressure to improve management and operational efficiency. The inability of many state monopolies to meet this challenge have given rise to policies of privatization of state monopolies and to the increased participation of foreign ownership and management.

7. Many countries are facing the need to formulate policies to deal with these issues. In this respect they might be greatly assisted by sharing the experiences of countries which have implemented policies of deregulation and privatization, as foreseen in item 3 (b) and 3 (c) of the work programme 1/ and the work of the Ad Hoc Group on Privatization.

B. The developed countries and the "services revolution"

8. In the 1970s, economists began addressing the phenomenon of the relatively greater growth in employment - and to a lesser extent GNP - generated by services (in comparison with that generated by manufacturing and agriculture) in developed economies.

9. In addition to high growth rates in services, there is also an increase in the value added incorporated into merchandise exports, and increases in human capital per worker (education and training) incorporated in goods. Trade in intermediate services is similar to trade in intermediate material goods in that both these types of intermediate inputs are indispensable to the production process and are often major sources of comparative advantage in manufacture for export. Furthermore, intermediate service inputs are used by all industries and their development is closely linked to the existence of comparative advantage based on other factors. 2/ To a certain extent, high growth rates in services may be explained by the income elasticity of demand for services, notably consumer services (entertainment, health, travel, tourism, etc.), as well as by the relatively low productivity of labour employed in the service sector. 3/ This type of analysis gave rise to concerns about the negative implications of the expansion of service sectors for the productivity of the economy, prospects for economic growth and sustained increases in real incomes (a process often termed "deindustrialization").

10. However, a second, more dynamic aspect to the service sector in modern economies concerns the major restructuring of the production process, of corporate strategy, and of labour markets. One manifestation of the evolution of the production process has been the emergence of the "producer services" sector as a growth sector of the industrialized economies. Professional business services had registered particularly high growth rates in the late 1970s and 1980s. This was quite marked in the United States of America where a relatively high proportion of new jobs was for the highly educated and well paid. Much of this can be explained by the implementation of information technology in the economy as a whole. Innovation is mainly by small specialist firms, a phenomenon better developed in the United States, accounting for their large growth rates in this period. Legal services, for example, grew by 106 per cent between 1980 and 1991, and business services by 67 per cent. 4/

11. The result is a process of feedback between technological progress and specialization. The demands of a more competitive environment (which, in turn, results from internationalization and deregulation) provide the necessary stimuli for technological progress to focus its creativity on developing new and better services, more "knowledge-intensive" and tailored closer to the requirements of the production and distribution processes. These new and enhanced services - generally associated with new information technologies - increase productivity for both goods and other services. They also facilitate the application of new management techniques, make relations between the various stages of design, production and marketing of products and services more expeditious, allow customized services to appear, help to generate greater economies of scale and facilitate an efficient globalization of the production and distribution functions. Competition - increasingly

based on access to and adaptation of technology - has provoked a growing demand for producer services. Technological progress has paved the way for a high degree of specialization while streamlining operations and the management of production units. The producer service sector lies between the infrastructure and the producer. The role of producer services is to assist the producer in using the infrastructure and in adapting technological advantages to specific needs. Analysis of employment in the service sector in the industrialized countries has demonstrated a dual structure with one component characterized by low wages and low-skilled part-time work, and the other - mainly the knowledge-intensive producer service sector - consisting of high skills and creative activities closely linked to the needs of the manufacturing sector.

12. The central manifestation of this phenomenon occurs with the "externalization" of a vast range of services which are required as inputs to the production and distribution of goods. These had hitherto been provided from within the production unit. Externalization has taken place at two levels. First, services produced internally are increasingly replaced by "outsourcing" (the purchase of specialized services from other firms). Secondly, the internal services operations of enterprises have been sold to outside customers, a process that has led to the establishment of subsidiaries which then sell their services both to the parent enterprise and to the open market ("spin-off" effects fed by accumulated knowledge and experience in the parent firm). This trend has been stimulated by the following factors: (a) the outside firms can make themselves more efficient through specialization; (b) staff cuts and outside production reduce the fixed operating costs of an enterprise, including those of training persons in the application of new technologies; (c) firms resort to acquiring licences or purchasing technology in order to produce savings on research and development (R&D). 5/ Information technology facilitates the operation of small and more specialized production units and firms.

13. In most of the developed countries, technological progress and greater competitiveness have been the cause and effect of the trend towards deregulation and/or simplification and updating of the regulatory machinery, making possible a more flexible and more adaptable integration of services into productive functions. Furthermore, with the growing complexity of service activities, the role played by Governments as providers of basic services is shrinking; their place is being taken by private agents. In this new context, Governments retain for themselves the important role of regulators, 6/ ensuring the sound operation of markets and the protection of consumers. 7/ This development is transforming relations between suppliers and users of services. First, it facilitates the emergence of a range of new services, which were much less available in the market until recently (because they were internalized); secondly, it generates a new demand for those services which have now been externalized. This is a basic characteristic of the externalization of services and the development of specialized firms capable of supplying efficient and innovative services at more acceptable prices and offering higher standards of quality and reliability. The new firms providing such services, in turn, can maximize profits through economies of scale and the scope derived from their different form of organization. 8/

14. New information technologies have rendered many services increasingly tradeable. "Knowledge-intensive services" can be exchanged through telecommunication networks. More and more people are crossing international frontiers either to render or to receive services. The opening of branches and subsidiaries of service firms or the provision of services through franchising and other management contracts is being facilitated by improvements in international information networks ("networking"). Little of this is reflected in conventional international trade statistics. Many transactions go unrecorded, despite the fact that they are an important component of the total revenues of enterprises and individuals. The establishment of international networks has led to substantial economies of scale and of scope; greater value added is created; many of the limitations hitherto imposed by the exigencies of direct personal contact between users and providers are eliminated. 9/

15. These developments have greatly enhanced two new dimensions of services: first, the proper integration and utilization of modern and efficient producer services in the production process is a key ingredient of competitiveness, both for firms and for the economy as a whole; secondly, producer services have become an important, if not the main, source of value added. This fact is partially reflected in the national accounts, especially of developed countries, by the growing share of producer services in GDP. These two factors lie at the heart of what is called the "services revolution". 10/

C. The new services economy and the developing countries

16. According to balance-of-payments results, countries may be grouped under three categories in terms of the role of services in the external sector. The first group comprises a large number of exporters of raw materials, which usually show a surplus in trade in goods and a deficit on services. A second group consists of countries which show a deficit in trade in goods and in most "other services", but surpluses under the heading of "workers' remittances" and "travel", activities which depend on the international movements of persons. The third group is smaller and includes a few Asian countries which have shown rapid economic growth. Their surpluses on services had previously offset their deficits on goods, although in recent years rapid growth in the export of manufactures has demonstrated complementarity between the two flows - exports of services support exports of goods; exports of goods support those of services. 11/

17. A general conclusion may be drawn from the foregoing: in many developing countries, services do not make a positive contribution to the external sector except where there are benefits from an active international movement of persons arising either when their own nationals render services ("workers' remittances") or when others act as consumers of their services ("travel"). Furthermore, countries with more vigorous growth in exports of manufacturers exhibit traditional strength in their trade in services. The characteristics of the international services trade of the developing countries appear to reflect the internal weaknesses of their goods and services sectors. An inadequate infrastructure, especially of telecommunications, and the lack of trained personnel have impeded the diffusion of new technologies, delaying the establishment of structures through which knowledge and "know-how" are disseminated, and customized services to suit specific enterprises' needs are

created and developed. This situation has delayed the domestic development of many producer services, increasing their reliance on "imported" services (often imported through subsidiaries or branches of transnational corporations) whenever foreign exchange availabilities permit.

18. Another aspect of the problem relates to the slowness of the "externalization" process for many producer services and the marked absence of domestically produced "knowledge-intensive" services. Excessive centralization in the operation of corporations or the existence of closed intra-firm circuits prevents the generation of an active and vigorous demand for such services. Furthermore, it keeps knowledge of, and access to, certain services captive within big corporations. The existence of accumulated "locked-in" knowledge amounts to a squandering of resources by inhibiting the fruitful use of positive externalities by the rest of the economy. Slowness in "externalization" means isolating these functions from market signals. Supply and demand forces are ignored, diminishing the potential of producer services for higher productivity, greater competitiveness and more value added, both at the firm level and at the national level.

19. In contrast to what has happened in the developed countries, many developing countries have still not managed to join the "services revolution". Thus strengthening competitive services in the developing countries is a matter of overcoming the problems presented by financial shortages, under-utilization of market mechanisms, insufficiently qualified human resources and inadequate access to new technologies.

II. Producer Services in Developing Countries

20. Increased competition based on trade liberalization, combined with technological advance, creates demand for both efficient infrastructural services (as noted above) and producer services. In developed countries, the producer services sector has evolved autonomously, conducted by the firms themselves – based on competition-driven demand and technology-driven supply. Demand has thus stimulated the need to adapt to competition in the domestic market and to take advantage of export opportunities. The supply of producer services comes from knowledgeable individuals who are capable of adopting technology and of using the infrastructure. To a large extent, the supply of services in developed countries has emerged from the manufacturing and agroprocessing sectors through the process of externalization.

21. The contribution which producer services make to competitiveness in the goods-producing sectors and to the overall economy in the developing countries may well be affected by the speed at which these countries have been brought into a much more competitive international setting. Most of the developing countries that have carried out programmes of structural adjustment, including liberalization of their regimes for both trade and investment, have done so in short periods of time and under pressure from outside. This has rendered more difficult the adaptation of domestic supply to new demands for producer services and the possibilities of their being produced by national firms. This contrasts with the situation in developed countries where autonomous adjustment carried out over several decades has enabled knowledge-intensive producer services to evolve and "spin off", as described above. Likewise firms could gradually and autonomously incorporate producer services into

their operations pari passu with technological changes and transformations in the organization and management of production required in a more competitive environment.

22. The increasingly competitive setting in which the developing countries' economies are evolving has acted mainly as a stimulant to demand for producer services. Owing to the absence of sufficiently skilled persons, managerial attitudes biased against externalization, inadequate infrastructure, inadequate access to technology and the (correct or incorrect) perception that domestic service suppliers are inadequate for various reasons, the domestic supply of such services has not always been able to evolve naturally to meet this growing demand. This has forced enterprises to make use of imported services. The effect is to reduce the chances of keeping the value added generated by producer services, especially in tradeable sectors where the incorporation of efficient and competitive services is crucial to their survival.

23. UNCTAD has supported a series of national and regional studies on the state of producer services in various developing countries. Some of these studies have concentrated on the demand for producer services generated by some productive activity of particular interest to a given country, 12/ while others addressed aspects of the supply of producer services. 13/ Other studies approached the review from the standpoint of both supply and demand. 14/ All these studies, however, form no more than a starting point from which to examine the situation of producer services under particular conditions. Research could be explored more thoroughly, through methodological development, the improvement of statistics and the pursuit of specific research projects.

24. The particular situation of a group of least developed countries, characterized by serious difficulties in terms of telecommunications, human resources, physical infrastructures and, in some cases, even unfavourable geographical location, is being examined by studies in progress. These could be used to produce a more comprehensive report in the future. 15/

25. The examination of the qualitative and quantitative aspects of the supply of, and demand for, producer services in different sectors of production provided information with respect to: degree of internalization and externalization of services; their market structure; competitiveness level; and the internal and external obstacles confronted by suppliers and consumers in the home market. The methods applied in these studies are far from uniform, making comparative analysis a difficult matter. There are substantial differences in such factors as sample size, classification of firms, sectors, features and level of replies obtained.

A. Demand for producer services

26. To a large extent producer services are essentially demand driven, generated by the needs of other sectors of the economy, including service sectors. Producer services will be in demand to the extent that the activities using such services operate in a setting that is vigorous and competitive enough to require them. A perusal of the studies prepared by UNCTAD reveals the existence of a dual development of producer services in the

developing countries. In most of those countries, several modern economic activities which rely on technological change and which normally compete in the international markets coexist with other activities which are technologically backward and traditional in their managerial and hierarchical structures. The latter have traditionally benefited from protection, and have not undergone the productive transformations necessary for competitiveness in international markets.

27. It was found that many enterprises – potential demanders of services – resist change and maintain a high degree of internalization of services. There are various reasons for this, including: the low level of competitiveness at which they operate; the fact that the firm considers that its own staff interprets its needs better than outside suppliers; entrepreneurial failure to perceive the economic advantages of "externalizing"; the low level of assimilation of new technologies; concerns over confidentiality; lack of confidence in the reliability of outside suppliers; high cost and/or inadequate quality of available producer services, and absence of policies encouraging the entrepreneur to externalize particular services. Even so, many firms had expressed a desire to externalize certain services, especially the following: R & D, market research, legal services, repair, maintenance and hire of equipment, quality control, data, engineering and consulting services, transport, financial services and training. 16/

28. Producers in the developing countries studied have taken different approaches towards producer services. The extreme approaches are: (a) to maintain many service functions internalized (this has been possible mainly for large firms), and (b) to adopt a passive position and allow foreign firms to supply all the producer services with a consequent loss of autonomy, value added and no benefits in terms of learning or transfer of technology. Firms exposed to international competition are highly dependent on foreign service providers for obtaining high quality services. They acquire their services via internationally integrated chains, intra-firm arrangements, through branches of transnational corporations or through their own customers under subcontracts. An extreme case of reliance on imported services has been observed in certain textile and citrus fruit and pineapple processing concerns, where the producer takes an essentially passive attitude, often depending entirely on services provided by the buyer of its products. 17/ Services obtained from such single buyer include design, quality control, international marketing and management consulting.

Box 1

Grouping of Producer Services according to the Production Function

In the administrative function, comprising bookkeeping, auditing, legal services and planning, internalization increases with the size of the enterprise. In many cases, reasons of strategy and confidentiality are given, especially in the case of large-scale enterprises. Small enterprises tend to internalize such services less, for reasons of cost; they are generally performed by one individual. Large-scale (and some medium-sized) enterprises have specialized departments.

The technical services function includes the services of engineering, R & D, quality control, maintenance and storage. These functions, which are of vital importance regardless of the size of the enterprise, are lacking in many small and medium-sized enterprises. Sometimes, where they are performed at all, this is done by the workers themselves. The large-scale enterprise in which such services are well structured is a case apart. In many sectors, R & D and quality control are non-existent or of poor quality for lack of skilled professional workers. Some industries report that this situation has affected their ability to adjust the supply of their products to the requirements of demand, in both local and foreign markets. In the sectors where there are foreign partners, these services, although internalized, are rendered under the guidance of outside firms. A striking case is that of subcontracting in offshore processing activities. These activities develop a kind of "passive" entrepreneur, for many of the functions are performed virtually entirely by the subcontractor. Something similar happens with the sale of engineering services, which are provided as "after-sales" services by the enterprise selling the equipment or machinery.

The functions of services connected with presence in the market include, among others, marketing, export services and transport. Transport forms an exception; the remaining services are highly internalized, especially where production is aimed at the home market. Export services present contrasts. In some large and medium-sized enterprises, marketing is carried out in the enterprise itself with the support of State agencies; in others, as in the case of subcontracting and enterprises with foreign partners, marketing is integrated in the trading partners' chain. Small and medium-sized enterprises report as a crucial problem of access to foreign markets, the lack of commercial information and the training of staff to equip them to pursue commercial information-gathering in foreign markets. Trading companies fill this gap in some countries.

Source: "Tunisia: National Study on Services", (mimeo).

B. Main characteristics of the supply of producer services

29. Much of the demand for producer services in developing countries has been met by foreign service providers, explaining the lack of vigour characterizing the supply of national producer services in the developing countries studied. Integrated systems of services applicable to production have not evolved; the connections between services and other sectors are not generally

perceived. 18/ Small and medium-sized enterprises in some categories of producer services are often perceived to be weak in respect of their ability to: 19/ (a) respond to the needs of the market and take advantage of them by offering more efficient services at lower cost than their competitors; (b) design, adapt and establish their operations at high levels of efficiency and productivity; (c) recruit and train highly skilled staff; (d) assimilate, adapt and apply new technologies that will enable them to reach higher levels of efficiency, productivity and competitiveness; (e) identify exportable services and foreign markets; (f) generate or obtain financing and working capital; (g) face strong competition from foreign suppliers or from State or semi-State monopolies. In addition, they sometimes operate in an inadequate regulatory system and an unfavourable economic environment. For all these reasons, these enterprises often survive by serving "second-class" customers in the home markets without any possibility of competing in international markets.

30. More than half the firms surveyed were less than five years old, generally low in efficiency and productivity, and had to compete with a few large-scale firms enjoying a large market share and generally some foreign capital. The latter firms can thus develop high-quality services at relatively low cost. This applies to accounting and auditing services, advertising, services providing information on value added, specialized consulting and financial services as well as services assembling and operating information networks. Many of the large firms are branches of foreign enterprises or national enterprises operating under various types of agreements such as franchises, exploitation of registered trade marks, patents, etc.

31. A feature of particular interest in the generation of a larger supply of services was observable in certain processing industries and others connected with the extraction of natural resources. In these cases, the main producers had generated their own service enterprises which, in addition to meeting the needs of the main firm and of others in the home market, had also begun exporting. 20/

32. The producer service sector can provide employment for skilled persons, particularly those who are conversant with new information technologies.

PART TWO

COMPONENTS FOR A POLICY OF STRENGTHENING SERVICES IN THE DEVELOPING COUNTRIES

I. Domestic Strategy

A. Context

33. Policy options for fostering competitive services sectors in developing countries and for their gaining an increased share of international trade in services will have to confront the questions of (a) financial resources, (b) the use of market mechanisms, (c) human resources, (d) access to new technologies, and (e) the participation of foreign providers. These issues are discussed in the following paragraphs.

(a) Financial resources:

34. Generally speaking, Governments and enterprises in developing countries lack the financial resources needed to tackle the modernization of services, while external financing schemes commensurate with the needs are generally not available. These problems are exacerbated in the case of heavily indebted developing countries, where adjustment programmes have further reduced the already scanty resources available for the expansion and renovation of basic infrastructure and where firms have difficulty raising resources in foreign markets. The chronic shortages of financial resources in developing countries have seriously affected their investment capacity to develop services compatible with the requirements of an efficient modern economy. The situation worsens in the case of those sectors transformed by advanced technologies where costly investments are needed to update their operation and management, including modernizing the necessary infrastructure. By way of illustration: in maritime transport, containerization entails the modernization of cargo-handling plants; 21/ in banks and financial services, global transactions depend on investment in telematic technologies, while the expansion of customer services requires sophisticated electronic equipment; 22/ in telecommunications, the development of value-added services entails expanding the basic network and introducing fibre optic cables; air transport and tourism are facilitated by the establishment of networks of computerized reservation systems, the development of facilities suitable for multimodal transport and the expansion and improvement of infrastructure at airports to facilitate passenger traffic and cargo handling. 23/ Another dimension of this problem relates to the financial management of many service enterprises both public and private. Firms are unable to generate their own resources when they cannot maintain profitable levels in their current operations; those in heavily indebted countries are unable to tap domestic resources that would enable them to cover their requirements for investment and working capital. In the case of public enterprises, many Governments are adopting policies of privatization aimed at improving management while reducing the financial pressure on fiscal resources. 24/ New service firms, in particular those that are knowledge-intensive, usually lack sufficient tangible assets to be used as collateral for bank credits. Such enterprises generally regard their human resources as their main capital. 25/

(b) The use of market mechanisms:

35. The development of efficient and competitive services may be assisted by a better utilization of market mechanisms with respect to the allocation of resources, price determination and the appropriate use of supply and demand forces in the "clearing" of markets. This would help increase the financial soundness of many service operations. In many countries those mechanisms are still in limited use for several service activities. The reasons for this scant use of market criteria are varied and complex. To a certain extent they reflect Governments' commitment to complex and ambitious objectives of integral development. Thus, they create a wide gap between private and social return for many services. Many developed countries have narrowed this gap by the extensive use of cross-subsidization for many basic services. Developing countries cannot always make use of such a tool.

36. In other cases, the poor use of market mechanisms is reflected in the concentration of demand in a small number of large-scale, generally monopsonic, users. In others, large-scale enterprises became self-sufficient units through the vertical integration of their operations. A defective market structure is not necessarily connected with the State ownership of particular services or with the monopsonic nature of demand for them. Many services rendered by the private sector exhibit clear examples of market concentration on the supply side, which does not always contribute to a better and more efficient integration of services with the production process. This is the case for professional services such as: advertising; accounting and auditing; 26/ computer-related services and software; 27/ and insurance and banking. 28/

37. Better utilization of market mechanisms may be achieved through changes in the regulatory framework that affects market entry, the behaviour of firms and the establishment of monopolies. Regulatory mechanisms vary from country to country and from sector to sector. Market entry regulations range from the establishment of standards on professional qualifications to limiting the entry of operators through the granting of licences (e.g. air transport) or the establishment of public or private monopolies (e.g. telecommunications and public services). Regulations affecting firms' behaviour may include: price-fixing practices of utilities (electricity and water), limiting the range of services offered (banking and insurance) or restricting the geographical coverage of service providers (road and urban transport, banking). 29/

(c) Human resources:

38. Shortage of qualified human resources in many developing countries constitutes a major obstacle to the development and strengthening of competitive services sectors. Suitable educational facilities are essential in order to meet the personnel requirements imposed by the technological transformation of many services, especially in the area of higher technical education. Various studies emphasize the urgent need to increase educational investment, to improve curricula in line with the requirements of the productive sectors and to upgrade the quality of equipment and facilities of the educational system. 30/

39. Although many developing countries have relatively high literacy rates and in many cases have a substantial number of highly skilled professionals, 31/ there are still shortages of personnel properly qualified to perform a number of productive tasks. This has been observed in such varied services as hotel and passenger transport services, advertising, auditing, insurance, banking and other financial services and computer services. 32/ In many service activities, "on-the-job" training is almost the only recourse. This means that training must be decentralized in order to adapt it to local market conditions, facilitating both the dissemination of knowledge and skills to the industry and, at the same time, realizing the export potential of skills which are not being properly used.

40. In view of these considerations, some developing countries have taken advantage of the presence of transnational corporations to include commitments to train the local workforce in the agreements they conclude with those corporations. Joint ventures, management contracts and the like have proved to be efficient means to promote "in-job training" in tourism, 33/ computer services, 34/ construction services and others. Furthermore, a few countries have become successful exporters in these activities, making good use of their associations with foreign enterprises by including performance requirements which have contributed to raise the skills of their own manpower. It will be noted that the role of joint ventures in stimulating the development of service sectors in developing countries and promoting trade in services and their access to technology will be examined under item 3 (e) of the Work Programme of the Standing Committee. 35/

41. Few studies have analysed the contribution of transnational service corporations in the area of human resource development; the need for thorough case studies of this subject is accordingly plain. 36/ Other traditional problems of the developing countries in the matter of human resources arise in connection with brain drain. In most cases this problem is very costly for the developing economies. It may be solved in part by creating incentives to stem the loss of highly educated people and in other cases by creating sufficiently desirable conditions to attract skilled foreign professionals as a means of improving the human capital endowment of the country. 37/

(d) Access to new technologies:

42. Advances in technology permit the creation of new competitive advantages. For example, in maritime transport, and particularly with regard to containerization, new technologies allow the development of functions that determine overall competitiveness, such as computerized control of operations and the application of new organizational and administrative techniques, all of which are only possible when there is ready access to modern telecommunications technologies. The competitiveness and efficiency of maritime transport operators are largely determined by the availability of such technologies in the environments in which they function. Although developing countries are great users of containerization, their share as suppliers of these services is very modest. 38/ For audiovisual services, access to new technologies used in subtitling films for cinema and TV, film copying techniques and signal transmission systems based on the use of fibre optics, cable television, HDTV and others are essential in order to compete. 39/ In auditing services, access to new auditing and accounting

techniques are important to the competitiveness of enterprises. 40/ Many small firms from developing countries are not able to access such technologies and therefore find themselves ill-equipped to compete. A few countries have tried to circumvent this problem by stationing their staff abroad and carrying out programmes on the equipment owned by users of their services in other countries. 41/ In the case of insurance, it is increasingly clear that competitiveness is based on the design of highly sophisticated products, the development of new techniques for assessing industrial risks, the improvement of capacity to design reinsurance schemes and the improvement of distribution and data processing systems. All these functions are highly dependent on new technologies. Shortcomings in this area have impeded the development of insurance companies in several developing countries. 42/

43. A few developing countries have managed to accede to new technologies through special agreements concluded with transnational corporations operating in their territories. When the host countries' capacity for assimilation, adaptation and dissemination permits, the introduction of appropriate clauses in joint venture arrangements may facilitate access to new technologies. In many cases, however, their introduction is weakened by high market segmentation in which large service TNCs are the exclusive providers for other TNCs. This applies to many professional and business services as well as banking, insurance, transportation and others.

(e) Participation of foreign providers:

44. Increased participation of foreign service providers can contribute to alleviating financial restrictions, increasing competitiveness in domestic markets, training and improving human resources, promoting the transfer of technology in the field of services, and promoting access to international information networks and distribution systems. Conversely, there may be instances where foreign participation is seen as being in conflict with the attainment of a Government's macroeconomic and social objectives and its policies with respect to specific service sectors. Developing countries have demonstrated a desire to prevent foreign enterprises from gaining a disproportionate dominance in local markets, so as to stifle the development of domestic enterprises, particularly where new, knowledge-intensive services are concerned, to resort to unfair trade practices, to provoke an undesired impact on the balance of payments, (arising from the repatriation of profits, intra-firm transactions, the purchase of inputs abroad and/or the use of transfer-pricing among its various branches and subsidiaries). For example, it may be necessary to limit the reinvestment abroad of insurance premiums obtained in the domestic market 43/ or to offset the cultural impact of foreign audiovisual services, 44/ especially when their presence is associated with cartelization and anti-competitive practices. Particular policies are needed to deal with conflicts which may arise between the objectives of the transnational corporations and those of the host countries.

45. The foregoing observations demonstrate the need for thorough studies of the positive contribution that can be made by greater liberalization of international markets for services. Efforts should be made to ensure that their participation is not limited to cornering the most profitable segments of national markets, and thus impeding the development of efficient domestic

services but, on the contrary, to ensure that they become an agent for change and modernization in the markets for services of the developing countries.

46. The Uruguay Round General Agreement on Trade in Services presents a framework in which foreign service providers can have secure market access and national treatment through negotiated bound commitments included in the Schedule of Commitments. This framework also permits developing countries to limit such concessions to those sectors where foreign providers are deemed desirable for the development programmes, and to obtain specific commitments from the suppliers benefiting from such access as well as reciprocal concessions from their trading partners.

B. General framework

47. Governments have at their disposal a set of instruments with which to stimulate the development of competitive services sectors. Some of these - such as exchange, trade, fiscal and credit policy - fall within the scope of macroeconomic policies. Others may necessitate changes in the institutional and regulatory framework, while the attainment of more specific objectives may call for particular strategies aimed at positioning national enterprises in the international market.

48. Exchange rate management is a vital instrument for stimulating the competitiveness of any economic activity. Services, being intangible, are much more vulnerable to ill-conceived exchange policies, and consequently may be seriously affected by the maintenance of overvalued or undervalued exchange rates. In many cases, this phenomenon merely feeds the foreign currency black market, severely depresses activity, impairs the competitiveness of locally produced services and favours cross-border rendering of such services or their consumption abroad. Highly volatile exchange rates, in turn, discourage the pursuit of such activities in the local market by introducing large elements of risk. Tourism is an activity particularly sensitive to exchange rate instability. 45/

49. The incorporation of "imported" services to assist the attainment of the objectives of sustained development, whether by protecting the environment, 46/ facilitating access to new technologies, information networks and distribution channels or improving capacity for training and the generation of domestic know-how, may also be an important component of development policy. Such has been the experience in joint-venture-type arrangements for the development of the construction industry in some developing countries, which have facilitated both the temporary movement of manpower and the transfer of technology on favourable terms. 47/ In this case the objective is a mutually beneficial association between the foreign investor and the host country, specifying the parameters for the fiscal, credit and operational treatment of enterprises which are partly or wholly foreign-owned. Policies with regard to trade in goods have also had a marked effect on the evolution and development of services. Imports of equipment and inputs for various service activities, especially high technology products and those which support the telecommunications infrastructure, need a sufficiently liberal regime not to thwart the development of the services that depend on such inputs. 48/

50. The regulation of many service activities is not always adequate in developing countries. Some service activities have developed vigorously, precisely because standards and regulations have been laid down for them. For example, such services as auditing and bookkeeping benefit from the accounting standards which the State imposes on enterprises for tax or other purposes. The use of quality control services is often stimulated by the application of certification standards imposed by the State or by the sector's own trade associations on exporters of particular products. An appropriate legal framework for the protection of intellectual property is another normative consideration that may support the development and utilization of home-generated services. 49/ Regulations directed towards the protection of the environment are also giving rise to a new demand for what are essentially producer services in developing countries. 50/ The issue of regulations is to be studied in detail at a later stage under item 3 (b) of the Committee's Work programme.

51. In some services, especially those which are knowledge-intensive and consequently dependent on technological factors, the most successful experiences 51/ reveal that an important role is played by Governments in developing these activities for both the domestic and international markets. 52/ Direct subsidies, government procurement, tax incentives and other mechanisms are used by Governments for these purposes. Fiscal or credit support may be indispensable to overcome the problems of certain firms lacking physical assets with which to back their loan applications.

C. Specific strategies

52. Strengthening services entails devising and applying specific strategies to overcome the weaknesses characteristic of the basic infrastructure and of producer services in developing countries.

(a) Modernization of the telecommunications infrastructure

53. Most of the developing countries are implementing policies to modernize and upgrade basic infrastructures (e.g. telecommunications, ports, airports, highways, irrigation works, power infrastructure, etc.), to develop environmental protection services such as waste-water purification or the reduction of pollution in road and air transport, 53/ and to improve the country's human resource base by upgrading the education system. A modern and efficient telecommunications infrastructure capable of supporting – at low cost – the domestic and international development of such varied services as banking, transport and other services that are direct users of such networks is indispensable. 54/ The absence of such an infrastructure stifles the possibility of increasing a country's share in world trade in services, in terms of both exports to foreign markets and access to advanced imported services. A strategy followed by some countries to increase investment in telecommunications infrastructure (financing, equipment and expertise) has been the application of the BOT system, 55/ under which the responsibility for building and operating such networks is handed over to national or foreign private enterprise.

54. Some countries have used innovative schemes in privatizing telecommunication services in association with foreign capital. 56/ This

is reported to have yielded new management techniques, technological improvements, cost reductions and wider coverage of the services concerned. 57/

55. A matter of concern centres upon possible widening of the existing gap between the developing and the developed countries telecommunications. Whereas the former are still trying to catch up with the great technological leap brought about by the digitalization of telecommunications, the developed countries are already building the new fibre-optic networks that will enable them to transmit far more information, and far more complicated information, in pulses of light. Virtually every type of digitalized information can be transmitted in this way, whether in the form of images, sound or text, including that from high-speed computers. Information services will flow at different paces and volumes in developed and developing countries simply as a result of the differences in basic telecommunications infrastructure.

(b) Producer services

56. The fragility of the domestic supply of producer services and, to a lesser extent, the inability to express a demand for such services restrict the chances for adapting domestic economic activity to the requirements of efficiency and competitiveness in a vigorous and increasingly globalized economy. Producer services are the decisive link in the value added chain. 58/ With this in view, enterprises are developing "tailor-made" competitive strategies. These strategies are based on such factors as the competitive structure of the industry in which they operate, their position in that industry, and clear identification of their particular sources of competitive advantages. They are obliged to explore the possibilities of creating advantages by seizing the opportunities presented by new technologies, the new and changing requirements of their customers, the emergence of new segments or niches in industry, changes in the cost or availability of inputs and changes in government regulations. Furthermore, the strategies should be oriented towards gaining a position in good time to take advantage of structural changes, then perceive and pursue innovation and sustain the advantages over time.

57. Developing countries have launched programmes of structural adjustment in order to create a setting that is more favourable to greater competitiveness and efficiency in their enterprises; however, many of these adjustment programmes do not pay sufficient attention to the link between producer services and adjustment in manufacturing and agricultural sectors. The role of producer services is precisely that of assisting enterprises to attain the necessary flexibility to adjust to more competitive and uncertain situations.

58. Structural strategies for strengthening the development and competitiveness of indigenous producer services would thus include specific measures to stimulate both the demand for and the supply of such services. Since this demand is derived from the requirements of other sectors, the situation faced by those other sectors with regard to regulation and competitiveness will determine the vigour of demand for services, particularly from those sectors exposed to international competition. Furthermore, the structural change that is affecting economic activity as a result of pressure to conserve the environment is not merely changing the technological pattern

in such activity but is also expanding the demand for related services such as marketing, environmental management, auditing, technological and risk assessment, environmental monitoring and other auxiliary services such as product testing. 59/ This expanding demand is largely being met by foreign suppliers. Consequently, the great challenge lies mainly in stimulating the supply of services provided by nationals to meet those needs.

59. Experience shows that in order to stimulate the supply of domestic services, Governments have used various instruments. These include direct financial support (e.g. to make good a shortage of venture capital); 60/ fiscal and credit incentives (e.g. exemption from import duties on equipment, tax exemptions on royalties, accelerated depreciation schemes or subsidized loans); 61/ modification of the regulatory system to reduce or remove the boundaries between different services (e.g. integration of telephones, computing services and cable television to provide multimedia services through fibre-optic networks); 62/ and specific measures to avoid "destructive competition" or "market skimming" by foreign suppliers. 63/ Other components of the strategy to promote the supply of such services include incentives for the "externalization" of locked-in knowledge, 64/ and the establishment of service centres or training centres aimed at teaching national staff to render producer services. In some countries these centres are turning into veritable nurseries of new producer services enterprises.

Box 2

Producer Service Centres: An Example

An interesting experiment in effective articulation of supply and demand requirements consists in the producer services centres which have developed in the north-central region of Italy in support of the textile and clothing industry. In many cases these services centres are being developed with the joint support of the local public authorities and the trade associations of service-using enterprises. The existence of such services centres has made it possible to maintain a traditional production structure in those industries (generally based on the family unit) while achieving greater competitiveness for the products they generate.

Source: Flavia Martinelli, "Productive Organization and Service Demand in the Italian Textile and Clothing Districts: A Case Study", in UNCTAD, Services and Development Potential: The Indian Context (UNCTAD/ITP/22), pp. 275-322.

II. External Strategy for Developing Internationally Competitive Services

A. How to penetrate world markets: Improving conditions of access to the international market

60. In seeking to penetrate world markets, developing countries face a set of problems which have to be surmounted in order to increase their share of world service trade. Solutions will require an appropriate strategy of negotiation, in some instances with other Governments in a multilateral, regional or bilateral setting 65/ and in others with transnational corporations. The main obstacles arise in the contexts listed below.

(a) Concentration of markets and transnational corporations

61. The growing importance of transnational corporations commonly results in relatively few firms dominating many markets for services. For example, 41 per cent of the reinsurance market depends on only eight companies originating from developed countries. 66/ In engineering and design services, 70 per cent of the demand is concentrated in the developing countries, but 90 per cent of the supply of such services originates from the developed countries. 67/ Only six developing-country firms are on the list of the 20 leading enterprises in the air transport field. The 10 biggest advertising groups in the world all belong to developed countries, as do the 20 biggest management consulting enterprises, the 15 biggest accounting and auditing firms and the 15 biggest software producers. Of the 20 largest hotel chains in the world, only one belongs to a developing country. A similar concentration is found in audiovisual services, with most of the enterprises that finance and distribute entertainment products located in the United States. 68/ The United States, Japan, Germany, France, Italy, the United Kingdom, Canada and Switzerland were the countries of origin of 63 per cent of the first 1,000 banks and 78 per cent of their total assets (1988). With regard to world earnings from tourism, over 80 per cent are collected by Western Europe and the United States. Furthermore, the business of hotel chains and tour operators is dominated by a few enterprises from developed countries. 69/ While the advertising business is dominated by a few firms in the United States, the United Kingdom and Japan, the business of auditing and bookkeeping is managed by the "Big Six". As to audiovisual services, the United States alone occupies more than 50 per cent of world screen time. The seven largest American companies control 85 per cent of box-office takings and 66 per cent of the market for the sale and rental of videocassettes. These enterprises form the cartel known as the Motion Pictures Association of America. Next in importance after the United States of America are France and Italy, whose share of the world market is 13 per cent of the total. 70/ This high degree of concentration is often a consequence of the enormous volume of capital and the complex networks of interdependent organization needed to maintain technological advantage and to exploit several "products" simultaneously. Thus, for a set of services, for example advertising, auditing and management consulting, firm-customer relations are established on a worldwide scale, making it difficult for enterprises originating from developing countries to gain access to world markets.

62. A decisive factor in ascribing this leading role to the developed countries' services is the role of transnational corporations originating from those countries. In such markets, the structure of competition exhibits characteristics akin to oligopoly, with far-from-transparent trade practices, with a high prevalence of complex intra-firm relationships and high barriers to entry. The United States in particular, with its large and relatively homogeneous home market, is successful in exploiting innovation because the returns can come sooner and are potentially larger. Economies of scale are made possible by a large home market. Firms can profit sooner and on a larger scale from innovative products and practices. This is more difficult in the European Community market, fragmented by languages, customs, tastes and laws, where local variants are costly and slower to develop. In the case of developing countries the problems are even greater. Economies of scale for large profitable firms can become virtually unassailable once a critical mass has been reached internationally. This appears to be the main determinant of TNC dominance, and forms a virtuous circle difficult to emulate for late-comers to the market, and especially for those based in developing countries. For instance, major United States manufacturing or financing services TNCs demand high levels of service at their overseas locations from the same or similar firms that they deal with at home, whether they are operating in sophisticated markets such as the European Community, or in developing countries. With the rapid innovation in service products resulting from new technologies and know-how, it is easier for a large supplier to combine them in-house than for the client to purchase them from a variety of small firms and assemble them.

63. In many instances, developed-country firms benefit from financial support from the Governments of their countries of origin. For example, trade flows in construction services are clearly affected by the presence of a number of distorting factors such as heavy government subsidies to export enterprises, tied aid, external financing packages, and political and other pressures.

(b) Anti-competitive practices

64. The high concentration prevailing in the markets for services opens the possibility of anti-competitive trade practices being pursued by the corporations themselves. These also clog the functioning of the markets and exacerbate the difficulties of new firms, particularly those from developing countries, to enter world markets. This prevents a healthy development of competition and its benefits. It affects in particular the users of such services and keeps potential competitors from sharing in the markets. Similarly, the use of anti-competitive practices by certain transnational corporations can thwart the development objectives of host countries by impeding the correct application of tax and exchange policies and pursuing discriminatory practices with regard to prices.

65. The best-known cases may be found in sea and air transport. Certain restrictive trade practices have been dealt with in the Code of Conduct for Liner Conferences, although structural shortcomings persist to prevent developing countries from gaining a greater share in the carriage of bulk cargo. Similarly a high degree of control is exercised by transnational corporations through the vertical integration of their operations or through the requirement that contracts be drawn up exclusively in f.o.b. terms. 71/

In air transport, abuses of a dominant position are practised by travel agencies and airlines and predatory tariffs are used for eliminating rivals. Many abuses have been detected in connection with the use of computerized reservation systems (CRSs), to the point where the European Community has drawn up regulations for the use of such systems, clarifying the boundary between the requirements of access to information networks and the use of unfair competition practices. Similar actions have been undertaken by the United States; the International Civil Aviation Organization (ICAO) has prepared a Code of Conduct on this issue. 72/

66. Cartel-type arrangements designed to fix premiums and preserve markets are common in the insurance field. Certain transnational corporations which provide services to enterprises restrict the coverage of services rendered to the customers of one of their branches in order to avoid conflicts of interest with the customers of another of their branches in another country. 73/

67. Both the problem of market concentration and the use of restrictive trade practices are dealt with, albeit in a clearly inadequate manner, in the General Agreement on Trade in Services. Experience has shown that such practices can undermine the very credibility of multilateral trade arrangements. Hence there is a need to tackle these problems exhaustively, by creating mechanisms for damage compensation and dispute settlement that will be genuinely effective.

(c) Access to information networks and distribution channels

68. The crucial importance of telecommunication networks and access to distribution channels in the availability of many services has already been emphasized. Of great significance in developing competitive capacity for financial services is the establishment of information networks that make it possible to introduce new financial instruments and facilitate the use of new management technologies and interconnections with firms located abroad. In audiovisual services, for example, access to distribution channels is the key to being able to exhibit the products of other countries on domestic circuits that distribute cinema and television programmes. 74/ The development of services connected with tourism depends heavily on access to information networks and distribution channels assembled by airlines, travel agencies and hotel chains, where segmentation of the markets for tourism operators bars access to such networks and channels for many suppliers of services from developing countries. 75/

69. Ready access to participation in networks is the key to the development of exports in such sectors as banking, some professional services, air transport and computing services. 76/ Access to distribution channels has presented an even more complex case since the distribution chains began internationalizing, creating their own integrated networks which extend from the design of the product or service to the final consumer wherever he may be. Such networks confer very substantial competitive advantages. Furthermore, the difficulties of gaining access to such channels make it impossible to reach markets for audiovisual services, software, professional services, banking, insurance and others. Facilitating access to information networks and distribution channels for service enterprises in developing countries is an indispensable component of any effort to improve those countries' share of

world trade in services. The possibility of developing countries requesting access to networks from foreign suppliers as a condition for granting market access and national treatment commitments is provided for in articles IV and XIX:2 of the General Agreement for Trade in Services. Questions related to access to networks will be examined under item 3 (e) of the Standing Committee's work programme.

(d) Access to markets and restrictions on the international movement of persons

70. Commitments with respect to government regulations of various kinds which impede access to markets of services are being negotiated in the Uruguay Round. They have also been included in many regional trade agreements. In the negotiations with the Round, developing countries have been giving particular attention to obtaining commitments with respect to the movement of natural persons as suppliers of services.

71. As in trade in goods, those services with export potential in the developing countries are ones which are highly labour-intensive. One form of making use of this advantage has been that of exporting services through the temporary movement of service suppliers. External resources received through workers' remittances represent a fairly high proportion of the total exports of many developing countries. 77/ These involve a variety of skill levels including managerial, professional and technical categories. Restrictions on the movement of persons who do not reside abroad (e.g. software consultants, etc.) can also affect developing-country exports of services. For many developing countries, the international rendering of services through the movement of persons is the only possible way to share in international trade. The removal of obstacles affecting the export of services by means of temporary movement of persons from developing countries is essential. 78/

72. In professional services, problems relating to the recognition of professional qualifications can also present barriers to the export of services. 79/ Item 3 (h) of the Standing Committee's programme of work relates to the analysis and identification of possibilities for the developing countries to make better use of this potential. 80/

B. Increasing participation of developing countries in international markets: Elements for a strategy

(a) The framework

73. At the multilateral level, the Uruguay Round negotiations on a General Agreement for Trade in Services contemplates provisions to the effect that foreign service suppliers gaining access to developing countries' markets should accept conditions with respect to transfer of technology, training and access to their information networks and channels of distribution. 81/ In this framework, developing countries have sought to negotiate reductions in the regulatory barriers affecting exports of their services.

74. Services have already been included in various regional integration programmes among developing countries. Existing complementarities and cultural commonalities can enhance trade and competitiveness in services.

Exports to outside the region may be promoted through joint associations. Unified approaches can help to enhance the bargaining power of members; the pooling of resources can ameliorate the conditions for acquiring access to information networks, distribution channels and equipment necessary for infrastructural updating.

(b) Options of strategies

75. Developing countries recognize the need to stimulate their exports of services not only as a means of increasing their foreign-exchange earnings but as a way of stimulating employment, upgrading the skills of their human resources and strengthening the home services sector in general. In turn, through their link with trade in goods, exports of certain goods normally support exports of services and, conversely, the export of certain services helps in exporting more goods.

76. A strategy to increase service exports thus involves efforts to develop competitive service enterprises at the domestic level as well as minimizing barriers to enter into world markets. A competitive services sector may be strengthened by means of strategies directed towards: (a) stimulating services in which some comparative advantages can be deemed to exist; (b) enhancing their competitive strengths through application of specific policy measures, and (c) improving conditions of access to foreign markets through multilateral, regional and bilateral negotiations with Governments and transnational corporations on obstacles that limit export opportunities.

77. These strategies should be able to generate an increase in exports of services in service sectors where developing countries possess or are able to "create" comparative advantages. Comparative advantage in services may derive from factors which are not necessarily related to "natural" elements; in fact, many of them are conditioned by the level and quality of previous development. The quantity and quality of the resources allotted to R & D, the training of human resources, the level and development of technology and industry, the build-up of knowledge relevant to production, the size of the home market, and the nature and extent of regulatory system: all these factors affect the domestic and international competitiveness that many services can attain. This presents a challenge to the developing countries in deciding how to develop competitive services in circumstances where the relative strength of the industrialized countries in such activities is the outcome of their own history.

(i) <u>Stimulating services in which comparative advantages exist or can be created</u>

78. Comparative advantages in services scarcely differ from those in goods. Price, quality and timely reliable delivery are common factors affecting competitiveness in both goods and services. As in the case of goods, countries can exploit their existing inherent comparative advantages (derived from locational specificities or from resource endowments); they can also pursue a competitive position through specific strategies.

79. Developing countries normally enjoy comparative advantages in services deriving from one or more of the following factors: (a) inherent services

comparative advantages arising from geographical, historical or cultural factors (i.e. activities such as tourism, certain transportation services, translation services, educational services, even medical services depend heavily on such elements); (b) the relatively low cost of both skilled and unskilled manpower in developing countries also constitutes a source of inherent competitive advantage and consequently opens up prospects for those services which make intensive use of that factor (e.g. construction services, domestic services, agricultural seasonal labour, hotels, restaurants and many business and professional services which are labour-intensive). 82/ Several countries have formulated specific labour service export policies. 83/ They have included additional measures to raise the skill levels of labour exports, strengthened personnel training, built up information networks and developed new labour service exports 84/ while penetrating new markets. 85/ The identification of particular niches into which specific services can be fitted on competitive terms is also important as a source of information in developing the export of such services as film dubbing and subtitling, the digitalization of data, printing services, certain professional services and so on.

(ii) Developing competitive strengths

80. The share in trade in services of service suppliers is closely linked to their ability to build up competitive strength. Major factors determining competitiveness are: (a) financial capacity, (b) the ability to make effective use of telecommunications and information technologies, (c) accumulated knowledge, skills and reputation, (d) "networking" ability, (e) established relations between suppliers and buyers, (f) presence in major markets, (g) ability to offer a package of services, (h) domestic market size, and (i) appropriate government incentives. 86/

81. Many of these advantages will not turn into exports unless special measures are taken to permit enterprises to: diversify their offer, gain access to foreign markets by establishing their own channels of distribution; 87/ acquire the technologies needed in order to compete effectively; cover risks; and invest and modernize through the purchase of technologically advanced (often expensive) equipment.

82. The creation of competitive advantages can originate in the knowledge build-up in the manufacturing and agricultural sectors or the extractive industries. Such knowledge can be converted into exportable activities to the extent that it is externalized and organized in ways that facilitate penetration into foreign markets through adequate information and distribution systems being created. 88/ Another way of supporting the creation of competitive advantages is the export of packages of services from specified geographical locations either under offshore arrangements or from teleports or free zones. This can allow countries with inadequate telecommunications infrastructures to circumvent this limitation without having to invest in the modernization of the entire national network. Furthermore, many labour services – skilled and unskilled – can be exported via cross-border trade, thus avoiding the restrictions faced by other modes of delivery such as the temporary movement of personnel. The concentration of highly skilled staff, supported by a good telecommunications infrastructure, may attract resources for the development of knowledge-intensive services of the Silicon Valley

type. 89/ Some countries have set about gradually replacing their exports of goods by exports of services, stimulating the development of activities to meet the requirements of highly specific niches in the international market. 90/ Others promote the export of goods that incorporate the greatest content of national services, and develop strategies whereby the export of services is a vehicle for exporting more goods. 91/

83. An important source for the creation of competitive advantages lies in improving access to new technologies. Both traditional services (financial services and transport) and the new computing services are steadily making more intensive use of new technologies. These are, generally speaking, a strong source of competitiveness in many services, although in some cases they require heavy investment in the training of personnel or in special equipment (e.g. for handling containers in transport).

84. Another factor connected with the creation of competitive advantages is bound up with the improvement of human resources. Qualification of the labour force is essential in order to mobilize national talent for application to new and traditional productive activities. 92/ On-the-job training is normally one method which countries use to transfer knowledge from transnational corporations to national personnel. This type of action can be stimulated by means of fiscal incentives or by linking the conditions of access to the national market with the contribution made by transnational corporations towards improving the skill level of domestic human resources. 93/

CONCLUDING REMARKS

85. In conducting a comparative analysis of service sectors in developing countries with the objective of identifying policies to assist developing countries in developing and strengthening their competitive service sectors (mandated under item 3 (a) of the work programme), the Standing Committee will be able to draw heavily from previous work carried out by UNCTAD and synthesized in this note, as well as upon specific studies being carried out under item 3 (b) to 3 (k) of the work programme. In order to organize its work under the present item in a more systematic fashion, the Standing Committee might wish to consider linking closely the future work under the present item to work being carried out under other items in its work programme, as well as identify priority issues from within the work programme.

The Standing Committee may wish to examine the strategies and policies implemented by countries with a view to strengthening the competitiveness of their service sectors, based upon submissions by member States, including both developed and developing countries, and further studies by the secretariat.

Following the analytical aspects contained in items 3 (a) to (k) of the work programme, the Standing Committee may consider examining the strengths and weaknesses of developing countries in specific service sectors, based upon studies by the secretariat and supported by information provided by member States as well as by private sector entities and non-governmental organizations. In this exercise, priority

could be given to sectors deemed to have a major role in the development process, as well as those where developing countries may possess a comparative advantage and export potential.

In linking future work under the present item to other items in its work programme, the Standing Committee may wish to give particular attention to assessing the impacts of progressive liberalization and of service imports in the development of competitive service sectors, and to examining difficulties faced by developing countries which prevent them from increasing their participation in world trade in services, as mandated under item 3 (g).

Notes

1/ See UNCTAD, "Services in the World Economy", UNCTAD/TDR/8 (Offprint) 1989.

2/ H.G. Grubel, "Direct and Embodied Trade in Services", The Fraser Institute, Service project discussion paper 86-1, Vancouver, Canada, 1986.

3/ Technology, Trade Policy and the Uruguay Round, Papers and Proceedings of a round table held in Delphi, Greece, from 22 to 24 April 1989 (UNCTAD/ITP/23), Part II, report of the round table.

4/ T. Elfring, "An International Comparison of Service Sector Employment Growth", United Nations Economic Commission for Europe, Discussion Papers Vol. 2, No. 1, Geneva, 1992.

5/ Services in the World Economy (UNCTAD/TDR/8) (Offprint) op. cit.

6/ G. Russell Pipe, "Telecommunications Services: Considerations for Developing Countries in Uruguay Round negotiations", Trade in Services: Sectoral Issues (UNCTAD/ITP/26), pp. 49-111.

7/ UNCTAD VIII: Analytical Report by the UNCTAD Secretariat to the Conference (TD/358), chapter IV.

8/ Sieh Lee Mei Ling, "Producer Services Development and Trade: Malaysia and ASEAN in the Uruguay Round. July 1991.

9/ Albert Bressand, "Access to Networks and Services Trade: Uruguay Round and beyond", in Trade in Services: Sectoral Issues (UNCTAD/ITP/26), pp. 215-247.

10/ Producer services are rendered in the various phases of production from the upstream services, such as feasibility studies, market research and product design; to the onstream and parallel stages of production, such services as quality control, equipment leasing, accounting and personnel administration; through the post-production stages to downstream services, such as marketing, distribution, transport advertising, after-sales service and others.

11/ UNCTAD/TDR/8 Offprint, Chapter II.

12/ Studies were made for the Andean group, Mexico, Brazil, Chile, Argentina, Dominican Republic, Tunisia, People's Republic of China, Cape Verde, and Malaysia. More than 6,000 firms were covered by the surveys made for these studies.

13/ Sieh Mei Ling, op.cit. and the studies on Tanzania and Cape Verde.

14/ Studies of Mexico, Dominican Republic, Tunisia and China.

15/ Studies are in progress on Benin, Burundi, Cape Verde, Tanzania, and Uganda under the CAPAS project.

16/ UNCTAD, "Producer Services: China's Light Industry" (draft paper, March 1993).

17/ Examples of this situation are described in the studies on free zones in the Dominican Republic and the maquila industry in Mexico.

18/ Yu Wei-Chiang, He Mao-Chun, Zhou Lin, Yang Yulong and Lin Xiaomao, "China's Tertiary Industry: Problems and Prospects" (UNCTAD, draft paper, March 1993).

19/ These features were identified mainly in the studies of producer services in Malaysia, Mexico and Tunisia.

20/ Studies of producer services in Dominican Republic, Mexico and Tunisia prepared under national projects on services.

21/ L.M.S. Rajwar, "Trade in Shipping Services: India, Malaysia and Thailand", in Services in Asia and the Pacific (UNCTAD/IP/51), vol. 2, pp. 177-210.

22/ UNCTAD VIII: Analytical Report by the UNCTAD secretariat to the Conference (TD/358), chapter IV.

23/ Christopher Findlay and Peter Forsyth, "ASEAN Interests in Air Transport Services in the Uruguay Round", in Services in Asia and the Pacific (UNCTAD/ITP/51), vol. 1, pp. 321-362; see also Mexico: A Service Economy (UNCTAD/ITP/58).

24/ According to UNDP, 80 countries are carrying out privatization programmes involving the privatization of some 8,500 public enterprises in the past 12 years, most of them in countries of eastern Europe and the former Soviet Union. It is reported from various sources that the volume of all transactions involved in privatization came to $53 billion in 1992.

25/ Sieh Lee Mei Ling, "Producer Services Development and Trade ...", op. cit.

26/ Sieh Lee Mei Ling, "Professional Business Services in ASEAN and the Uruguay Round Trade Negotiations", in Services in Asia and the Pacific (UNCTAD/ITP/51), vol. 1, pp. 35-76.

27/ Mexico: A Service Economy (UNCTAD/ITP/58).

28/ Un Hoe Park, "Trade in insurance in Korea", in Services in Asia and the Pacific (UNCTAD/ITP/51), vol. 1, pp. 177-211.

29/ This enables them to provide services such as telecommunications, water, power and even transport and banking at rates accessible to users located in distant areas without damage to the enterprises' financial results.

30/ Dorothy Riddle, "Fostering the growth of new service exports from developing countries", in Services in Asia and the Pacific (UNCTAD/ITP/51), vol. 2, pp. 292-340, and Thierry Noyelle, "Computer software ..." op. cit.

31/ There are many examples of lawyers and other professional people in developing countries who are compelled to earn their living driving taxis or performing similar work.

32/ Chow Kit Boey, "International Trade in Tourism in ASEAN Region", in Services in Asia and the Pacific (UNCTAD/ITP/51), vol. 1, pp. 363-395.

33/ Chow Kit Boey, op. cit.

34/ Thierry Noyelle, "Business Services and the Uruguay Round negotiations on trade in services", in Trade in Services: Sectoral Issues (UNCTAD/ITP/26).

35/ Yehia Soubra, "Construction and Engineering Design Services: Issues Relevant to Multilateral Negotiations on Trade in Services", in Trade in Services: Sectoral Issues (UNCTAD/ITP/26), pp. 185-214.

36/ UNCTC, Transnational Corporations in World Development Trends and Prospects (ST/CTC/89).

37/ Paul Chan Tuck Hoong, "Trade in Services in Malaysia: Construction, Engineering and Medical Services", in Services in Asia and the Pacific (UNCTAD/ITP/51), vol. 2, pp. 127-176.

38/ L.M.S. Rajwar, "Trade in Shipping Services: India, Malaysia and Thailand", in Services in Asia and the Pacific (UNCTAD/ITP/51), vol. 2, pp. 177-210.

39/ Malati Tambay Vaidya, "Trade in Media Services: Asia and the Pacific Region" in Services in Asia and the Pacific (UNCTAD/ITP/51), Vol. 1, pp. 269-320.

40/ Thierry Noyelle, op. cit. pp.309-363,

41/ Thierry Noyelle, op. cit.

42/ J.F. Outreville, "Trade in Insurance Services", Trade in Services: Sectoral Issues (UNCTAD/ITP/26) pp.153-184; Un Hoe, op. cit.; and, Mexico: A Services Economy, op. cit.

43/ K. Sauvant and Z. Zimny, "Foreign direct Investment in Services: the neglected dimension in international services negotiations", in Services and Development Potential: the Indian Context (UNCTAD/ITP/22), pp. 71-112.

44/ S. Christopherson and S. Ball, "Media Services: Considerations relevant to multilateral trade negotiations", in Trade in Services: Sectoral Issues (UNCTAD/ITP/26)

45/ Françoise Vellas, "Approche du secteur de tourisme international", (consultant's report), UNCTAD, April 1993.

46/ Paolo Bifani, "Services and Environmental Protection", (draft paper) UNCTAD, May 1993.

47/ Yehia Soubra, "Construction and Engineering Design Services: Issues Relevant to Multilateral Negotiations on Trade in Services", in Trade in Services: Sectoral Issues (UNCTAD/ITP/26), pp. 185-214.

48/ Thierry Noyelle, op. cit. pp. 309-363.

49/ Arturo Borja T., Antonio González Vargas, Lourdes Hernández and Alvaro García Oramas, "Servicios de Software y Computación", México: una economía de servicios (UNCTAD/ITP/58).

50/ Bifani, op. cit.

51/ For example, engineering and construction services in the Republic of Korea, computer programming and software development in India.

52/ Overseas Construction Act of 1975, Republic of Korea.

53/ Paolo Bifani, op. cit.

54/ The developing countries, which represent 70 per cent of the world population and produce 20 per cent of the world GDP, use barely 7 per cent of the world's telephones. There are more telephones in the city of Tokyo than on the whole African continent.

55/ BOT: "Build, operate, transfer".

56/ Robert Devlin, "El proceso de privatización y lel bienestar social", (mimeo, March 1993) ECLAC, Santiago, Chile.

57/ Ibid.

58/ Sieh Lee Mei Ling, "Producer services, development and trade ...", op. cit.

59/ Paolo Bifani, "Services and Environmental Protection", Draft paper, UNCTAD, May 1993.

60/ In Colombia, the Government established the Vallejo plan, which includes a component for the development of service enterprises through soft financing for the purchase of equipment, international promotion and the acquisition of technologies.

61/ The Singapore Economy: New Directions, Report of the Committee, Ministry of Trade and Industry. Singapore, February 1986. The Government of Singapore established a programme aimed at supporting various producer services sectors such as: computer services, quality control services, professional services and hotel management.

62/ "Eyes on the Future", Newsweek, 31 May 1993.

63/ Flavia Martinelli, "Services, Trade and Development", Services in Asia and the Pacific (UNCTAD/ITP/51), vol. 2.

64/ This applies to Tunise Engineering et Construction Industrielle (TECI), established to make use of accumulated knowledge in phosphate and fertilizer mine engineering.

65/ Several economic integration schemes such as EEC, MERCOSUR and the Andean Group as well as free trade agreements such as NAFTA and ASEAN include arrangements for liberalizing trade in services.

66/ ReActions, March 1988.

67/ Engineering News Record, vol. 223, No. 6, 10 August 1989.

68/ UNCTAD VIII: Analytical Report, op. cit.

69/ Francisca Carner, "América Latina y el Caribe: El Comercio de Servicios en Turismo y las Negociaciones de la Ronda Uruguay" (mimeo).

70/ Francisca Carner, "El Comercio de Servicios Audiovisuales de América Latina" (mimeo).

71/ Peter Faust, "Shipping Services", in Trade in Services: Sectoral Issues (UNCTAD/ITP/26), pp. 113-151.

72/ Philippe Brusick, Murray Gibbs and Mina Mashayekhi, "Anti-Competitive Practices in the Service Sector", in Uruguay Round: Further papers on Selected Issues (UNCTAD/ITP/42), pp. 122-156.

73/ Thierry Noyelle, op. cit., pp. 309-363.

74/ Susan Christopherson and Stephen Ball, "Media Services: Considerations relevant to Multilateral Trade Negotiations", in Trade in Services: Sectoral Issues (UNCTAD/ITP/26), pp. 249-308.

75/ México: Una Economia de Servicios (UNCTAD/ITP/58).

76/ F. Vellas, op. cit.

77/ See TD/B/CN.4/24.

78/ Pang Eng Fong, "Labour Mobility, Trade in Services and the Uruguay Round: The Perspective of ASEAN Countries", in Services in Asia and the Pacific (UNCTAD/ITP/51), vol. 1, pp. 141-175.

79/ Paul Chan Tuck Hoong, op. cit.

80/ See TD/B/CN.4/27.

81/ UNCTAD VIII: Analytical Report, op. cit.

82/ Examples of good use being made of these advantages are found in some Caribbean countries, where in addition to taking advantage of the low cost of manpower, they also derive advantage from their language – English – and geographical proximity to markets of special interest.

83/ India, Pakistan and the Philippines have developed such policies to stimulate contract and individual labour exports by enacting legislation which covers recruitment criteria, length of employment, benefits, rewards and penalties, the issuance of permits and other necessary rules.

84/ Data processors in Caribbean countries are paid one tenth to one fifth of the salary of a similar worker in the United States of America. Cost accounting software systems for Lufthansa are designed by an Indian firm.

85/ Zhang Nigxiang, Chu Changyou, and Xu Dansong, "Labour Service Exports from China: Present Situation and Future Potential" (mimeo) Research Institute for International Economic Cooperation, Ministry of Foreign Economic Relations and Trade, Beijing, November 1992.

86/ M. Gibbs and M. Hayashi, "Sectoral issues and the multilateral framework for trade in services: an overview" in Trade in Services: Sectoral Issues, UNCTAD/ITP/26, pp. 1-48.

87/ For instance, China's labour services are exported by means of their international economic and technical cooperation companies (IE&TCC's).

88/ The decentralization of Petróleos de Venezuela stimulated the export of end-services for the engineering, drilling and maintenance of oil wells as well as services for the construction of road infrastructure. Codelco, a Chilean mining enterprise, gave rise to enterprises specializing in advanced engineering for copper, which is also being exported.

89/ Pyramid Valley in Egypt functions on this basis and aims to become a great regional supplier of computer services. The scheme is being developed jointly with the participation of transnational corporations.

90/ Emphasis on professional services such as: organization of trade fairs and exhibitions, consultancies and management services, design and know-how packages, furniture, electronics, turnkey projects for countries improving their technological bases. The Singapore Economy, op. cit.

91/ The export of engineering services normally supports exports of capital goods as in the case of the firm of Mendes Junior of Brazil under a telephone project at Lagos.

92/ The Singapore Economy, op. cit.

93/ It has been found that people retain about 10 per cent of what they see, some 20 per cent of what they hear, 50 per cent of what they see and hear and 80 per cent of what they see, hear and do. Newsweek, 31 May 1993.